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UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF PENNSYLVANIA

United States Fidelity and
Guaranty Company :
:
:
v.
:
:
Bruce J. Brown and Brown, Schultz
Sheridan & Fritz :
:

Judge Connor
MJS:mySCR
No: 01-CIV-813

FILED
HARRISBURG, PA

NOV 04 2002

MARY E. DANARE, CLERK
Per RD
Deputy Clerk

**EXHIBITS TO DEFENDANTS REPLY BRIEF IN SUPPORT OF ITS
MOTION FOR SUMMARY JUDGMENT**

Exhibit A	August 6 and 7, 2002 letter from K. Carson to Bruce Levin
Exhibit B	Plaintiff's Response to 8/7/02 letter
Exhibit C	October 16, 2002 Letter from Bruce Levin to Kathleen Carson
Exhibit D	Excerpts of T. Phillips Deposition
Exhibit E	Excerpts of J. Daily Deposition
Exhibit F	Excerpts of D. Hussey Deposition
Exhibit G	Excerpts of 7/19/02 Bruce Brown Deposition and Exhibit 19 thereto

Swartz | Campbell | Detweiler

Kathleen M. Carson
Attorney at Law

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August 6, 2002

VIA FACSIMILE

Bruce J. Levin, Esquire
Bernkopf, Goodman & Baseman, LLP
125 Summer Street
Boston, MA 02110

Re: USF&G v. Brown Schultz Sheridan & Fritz

Dear Bruce:

We request that you immediately produce Mr. DeBruyn's working paper files with regard to his opinions and report, including the restated financials attached as exhibits to his expert. Please advise us by close of business today if and when you will produce that information.

Very truly yours,

SWARTZ, CAMPBELL & DETWEILER

BY: *Kathleen M. Carson*

JEFFREY B. MC CARRON
KATHLEEN M. CARSON

KMC/kc

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August 7, 2002

VIA FACSIMILE

Bruce Levin, Esquire
Bernkopf, Goodman & Baseman, LLP
125 Summer Street
Boston, MA 02110

Re: USF&G v. Brown Schultz Sheridan & Fritz

Dear Bruce:

I write pursuant to Local Rule 7.1 and 26.3 to determine when Mr. DeBruyn's workpapers will be produced. In addition, I write to determine if you will agree to an amendment of the case management order regarding the timing of defendants' expert disclosures in light of the fact that Mr. DeBruyn's workpapers have yet to be produced.

First, Mr. DeBruyn's workpapers should have been produced with your expert disclosures on July 22, 2002 pursuant to F.R.C.P. 26. In addition, we also requested that this information in our last set requests for production directed to USF&G. We requested that USF&G

Produce any restated financial statements prepared by you or on your behalf with regard to CCI and any and all documents relied upon by you in connection with the preparation of those restated financials.

UFS&G's response was that the restated financials and all discoverable materials related thereto would be produced. However, to date we have not received Mr. DeBruyn's working papers or any other documents responsive to this request.

When we spoke at the depositions of Messrs. Daily and Silverstein on July 30, 2002, I

Bruce Levin
August 7, 2002
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requested that the working papers be produced. I did not receive a response to my request. I called you yesterday to discuss the production of this information and again today and have received no response from you. In addition, by letter dated August 6, 2002, I requested that you advise whether and when the work papers would be produced. Please advise us when we may expect to receive them as they are necessary for our expert's preparation of his report.

Finally, in light of USF&G's failure to timely produce the working papers, we request that USF&G stipulate to a thirty day extension of the deadline for production of defendants' expert reports. We would, of course, be willing to stipulate to a similar extension of the date for USF&G's disclosures with regard to its rebuttal experts.

Please advise us whether and when the working papers will be produced and whether you will agree to the proposed extension or if it will be necessary to file a motion with the Court.

Very truly yours,

SWARTZ, CAMPBELL & DETWEILER

BY: Kathleen M. Carson
JEFFREY B. MC CARRON
KATHLEEN M. CARSON

kmc/kc

B

10/16/2002 17:53 FAX

Bernkopf Goodman

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BERNKOPF, GOODMAN & BASEMAN LLP

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TELEPHONE (617) 790-3000

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October 16, 2002

Bruce D. Levin

DIRECT DIAL: (617) 790-3314

e-mail: blevin@bgblaw.com

VIA TELECOPIER

Kathleen Carson, Esq.
Swartz Campbell Detweiler
1601 Market Street
Philadelphia, PA 19103-2316

**RE: United States Fidelity & Guaranty v. Bruce J. Brown et al.
M.D. Pa. No. 01-00813**

Dear Kathleen:

I would like to formerly designate the following as constituting expert reports (and supplements thereto) regardless of whether previously designated as such:

1. Expert Report of Steve J. DeBruyn, CPA, dated July 22, 2002;
2. Supplemental and Rebuttal Expert Report of Steve J. DeBruyn, CPA, dated September 20, 2002;
3. Affidavit of Steve J. DeBruyn, CPA in Opposition to the Defendants' Motion for Summary Judgment, dated October 8, 2002 (served October 9, 2002);
4. Expert Report of Richard D. Farnsworth, dated September 20, 2002; and
5. Affidavit of Richard D. Farnsworth in Opposition to the Defendants' Motion for Summary Judgment, dated September 27, 2002 (served October 9, 2002).

The designated reports are subject to and without waiver of any rights we have to serve further supplementations of these reports.

Please feel free to contact me if you have any questions.

10/16/2002 17:53 FAX

Bernkopf Goodman

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BERNKOFP, GOODMAN & BASEMAN LLP

Very truly yours,

Bruce D. Levin / MVB
Bruce D. Levin

BDL:alb

cc: Peter B. McGlynn, Esq.
Mark Holtschneider, Esq.

#255189 v1/36432/87

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Tony Phillips (Vol. II) - 5/29/02

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VOLUME II

2

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

3

4

UNITED STATES FIDELITY
and GUARANTY COMPANY

5

Plaintiff

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vs.

CIVIL ACTION NO:
NO. 1-01-CV-00813

7

BRUCE BROWN and BROWN,
SCHULTZ, SHERIDAN & FRITZ

8

Defendants

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The deposition of TONY PHILLIPS was held on
Wednesday, May 29, 2002, commencing at 10:20 A.M., at
the Law Offices of The St. Paul Companies, 5801 Smith
Avenue, Baltimore, Maryland 21209, before Ronda J.
Thomas, Notary Public.

16

APPEARANCES:

17

PETER B. MCGLYNN, ESQUIRE
On behalf of Plaintiff

18

19

JEFFREY B. MCCARRON, ESQUIRE
On behalf of Defendants

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REPORTED BY: Ronda J. Thomas, RPR

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<p style="text-align: right;">226</p> <p>1 STIPULATION 2 It is stipulated and agreed by and between 3 counsel for the respective parties that the filing of 4 this deposition with the Clerk of Court be and the same 5 is hereby waived. 6 ----- 7 Whereupon, 8 TONY PHILLIPS, 9 called as a witness, having been previously duly sworn 10 to tell the truth, the whole truth, and nothing but the 11 truth, was examined and testified as follows: 12 MR. McGLYNN: Same stipulations we had 13 previously. 14 EXAMINATION BY MR. McCARRON: 15 Q Mr. Phillips, you realize you're still 16 under oath from the last time we had your deposition; 17 is that right? 18 A Yes. 19 Q You were previously deposed on April 17, 20 2002, in connection with this case; is that right? 21 A Yes.</p>	<p style="text-align: right;">228</p> <p>1 A I believe the initial approval of the bond 2 program for CCI was made by Jim Daily and John Huss. 3 Q What was the position/title of John Huss? 4 A Vice president. 5 Q Once the bond program was established for 6 CCI Construction who had the ultimate authority about 7 whether to commit USF&G to bond particular contracts 8 for CCI Construction? 9 MR. McGLYNN: Initially? 10 MR. McCARRON: Well, once the program got 11 up and running who then had the ultimate 12 responsibility, ultimate authority about whether to 13 commit USF&G to bonds. 14 A There were various authority levels 15 depending upon the job size and program. 16 Q Who, though, at USF&G had the ultimate 17 authority about whether USF&G would commit to bonds for 18 CCI Construction contracts? 19 A Depending upon the job size and program 20 there was various levels of authority given to the 21 branch or above those levels would have to be referred</p>
<p style="text-align: right;">227</p> <p>1 Q On that occasion I asked you questions and 2 you provided answers; is that right? 3 A Yes. 4 Q You realize you were under oath at that 5 time; is that right? 6 A Yes. 7 Q You realize you're now still under oath 8 just as you were on April 17th, 2002; is that right? 9 A Yes. 10 Q Did you review your deposition from 11 April 17, 2002 before today? 12 A Yes. 13 Q Did you notice any information or answers 14 which you provided on April 17, 2002 in that deposition 15 which you believe was either incorrect, wrong or 16 incomplete? 17 A There were a few words that were 18 mispronounced or spelled wrong. The general scope of 19 the answers were all correct. 20 Q Who made the initial approval of the bond 21 program for CCI on behalf of USF&G?</p>	<p style="text-align: right;">229</p> <p>1 to the home office. 2 Q So was it the situation that the field 3 office which you worked had a limited authority to 4 approve individual bonds within the bond program for 5 CCI Construction once the bond program was established? 6 MR. McGLYNN: Objection. You may answer. 7 A Yes. 8 Q Was there any occasion when the field 9 office did not approve a bond for CCI Construction? 10 A I can't think of any. 11 Q If the field office did not approve a bond 12 for CCI Construction was there a means by which CCI 13 Construction could obtain approval for USF&G to commit 14 to a bond? 15 MR. McGLYNN: Objection. You may answer. 16 A That's hypothetical. I couldn't give an 17 answer to that. 18 Q Well, if you or someone else in the field 19 office of USF&G refused to approve a bond for CCI 20 Construction would that have been the final word that 21 USF&G would not have issued the bond?</p>

2 (Pages 226 to 229)

Tony Phillips (Vol. 1, - 5/29/02)

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1 Q So to understand the extent of the revenue
2 generated from a warranty claim you would have to ask
3 further -- you would have to ask questions to obtain
4 additional information?

5 A If that was important to us, yes.

6 Q Did you ever do that?

7 A If that was important to us.

8 Q Did you --

9 A I never did that because as of the date you
10 make reference to here it wasn't important to us.

11 Q Was it important on any other occasion
12 which prompted anyone affiliated with USF&G to
13 determine the extent to which income was actually
14 derived or revenue was derived by CCI from a PCIC
15 warranty paid claim?

16 A It might have been to the extent that there
17 was a substantial amount of warranty income generated
18 against a substantial losing operations of CCI that
19 would have a net effect of showing say a slight profit
20 then questions probably should have been asked at that
21 time.

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1 was it ever determined it was important to know the
2 extent to which revenue was derived by CCI from a
3 warranty claim?

4 MR. McGLYNN: Objection.

5 A If it was so substantial corresponding to a
6 loss of income from construction operations that it
7 would jump out and grab a person who would be looking
8 at the financial analysis, then it would have become
9 apparent which I believe it never did.

10 Q I'm showing you a document Phillips
11 Exhibit 5 which is the 1998 and 1997 financial
12 statement and on page 13 footnote eight it's titled
13 related party transactions; isn't that true?

14 A True.

15 Q Now, did you read the footnote eight
16 included within Phillips Exhibit 5 when you received
17 the financial statement during your work for CCI bond
18 program?

19 A Possibly. Although the financial statement
20 was analyzed by Steve Salazar.

21 Q Well, did you depend on Steve Salazar to

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1 Q Does that mean no, no one ever asked about
2 the extent to which CCI received revenue because of a
3 warranty claim paid by PCIC?

4 MR. McGLYNN: Objection.

5 A No one ever asked.

6 Q Was it ever important to know the extent to
7 which revenue received by CCI was derived from a
8 warranty claim paid by PCIC?

9 MR. McGLYNN: Objection, asked and
10 answered.

11 A To the extent that the company had
12 sufficient cash, working capital, net worth and what we
13 believe was profitable operations going forward, it was
14 not that important.

15 Q Does that mean no it wasn't important for
16 USF&G to determine the extent to which revenue was
17 received by CCI from a warranty claim?

18 MR. McGLYNN: Objection.

19 A Depending upon the circumstances at the
20 time it was not that important.

21 Q Well, what does it depend on? I'm asking,

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1 personally analyze the information included within the
2 financial statements?

3 A Yes.

4 Q Including the financial statement for the
5 years ending December 31, 1997 and 1998 which is
6 Phillips Exhibit 5; is that true?

7 A True.

8 Q Now, did you read the last paragraph under
9 footnote eight in or about the time you received the
10 financial statement, which is Phillips Exhibit 5, which
11 reads in addition Pennsylvania Contractors Insurance
12 Company has guaranteed a claim of \$1,162,460 filed by
13 the company with a contract owner. If the owner fails
14 to pay all or any part of this claim, the insurance
15 company will pay the unpaid portion?

16 A I personally don't remember that. My
17 underwriter may have.

18 Q Did Mr. Salazar bring to your attention
19 that for 1998 the financial statement of CCI
20 Construction included in its revenue amount \$1,162,460
21 which was based on a guarantee from PCIC in case the

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1 owner didn't pay?

2 A I don't believe it was included in revenue
 3 where it should have been. So I don't think he caught
 4 that.

5 Q Was it included, sir?

6 A No.

7 Q Well, was there any -- if you had read this
 8 paragraph which starts out in addition PCIC has
 9 guaranteed a claim of \$1,162,460, would you have
 10 understood it?

11 MR. McGLYNN: Objection.

12 A Possibly.

13 Q Well, why wouldn't you have understood what
 14 the last paragraph indicates?

15 MR. McGLYNN: Objection.

16 A I'm looking at this in little more than a
 17 precursory review and looking at the notes and seeing
 18 that an insurance company is guaranteeing a claim with
 19 a contract owner. I don't know what claim that would
 20 be. It says that the insurance company will pay the
 21 unpaid portion. I don't know the parameters of PCIC as

1 warranty payment or the guarantee rather is for a,
 2 which you thought was going well or not or you didn't
 3 know whether it was going well?

4 MR. McGLYNN: Objection.

5 A I don't think when my underwriter analyzed
 6 that he put together anything regarding the fact that
 7 this was related to a construction job that was going
 8 bad.

9 Q And why not?

10 A There was not sufficient notes. There was
 11 not sufficient scheduling to show that these two were
 12 related to a specific job or jobs in which it would
 13 state the actual jobs in process identified as job
 14 number this, job number this, job number that were
 15 showing the following additional cost which would have
 16 been picked up by this policy. If that was the case
 17 then it would have raised a red flag.

18 Q Well, you didn't know one way or the other
 19 did you, from that statement?

20 A It wasn't asked.

21 Q And you didn't ask the question?

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1 to whether or not they had a fire policy in effect, a
 2 liability policy or what policy in effect that would
 3 allow them to do that.

4 Q Would it be important for you to know that
 5 information?

6 MR. McGLYNN: Objection.

7 Q That is the basis and reason for the claim
 8 guaranteed by PCIC?

9 MR. McGLYNN: Objection.

10 A It would be important.

11 Q Did you ask the question --

12 MR. McGLYNN: Let him finish.

13 Q I'm sorry.

14 A It would be important if we had reason to
 15 believe that it was reflected or reflective of a
 16 construction job or construction jobs that we believed
 17 were at least going okay that were deteriorating as to
 18 lost profits or increased losses. If there was a note
 19 to that effect then it would be important to us.

20 Q So is it unimportant to you simply because
 21 it doesn't reflect one way or the other whether the

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1 A No.

2 Q But you had no comfort in knowing that
 3 1.162460 amount was for any particular job, did you?

4 MR. McGLYNN: Objection.

5 A If you're asking me in that standpoint, I
 6 don't know what my underwriter thought in that regard.

7 Q Yeah, but the underwriter is under your
 8 management and supervision, right?

9 A Yes, and I'm under -- at the time I'm under
 10 Mike Walter's supervision who's under Jim Daily's
 11 supervision who's under somebody else's supervision and
 12 to the extent that we are looking at an overall
 13 picture.

14 We're looking at income that is profitable.
 15 We're looking at cash, working capital and net worth

16 which we feel is sufficient. We didn't put together
 17 the fact that that one sentence or two sentence notes
 18 would have been reflective of a change in accounting
 19 principles or procedures or etiquette to show that some
 20 particular job which had unrecognized cost would be
 21 guaranteed if they weren't paid.

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<p style="text-align: right;">374</p> <p>1 Q You didn't think it was significant about 2 whether there was a valid source of payment for 3 \$1.162 million for CCI?</p> <p>4 A As I said --</p> <p>5 Q During 1998?</p> <p>6 MR. McGLYNN: Let him finish.</p> <p>7 Q I'm not finished my question.</p> <p>8 MR. McGLYNN: Well then don't raise your 9 voice.</p> <p>10 Q During 1998 when it already had -- you 11 learned halfway through the year it was losing or had 12 lost \$1.6 million?</p> <p>13 A Was that important to --</p> <p>14 Q Yes.</p> <p>15 A -- the bottom line?</p> <p>16 Q Yes.</p> <p>17 A Yes, it was important to the bottom line.</p> <p>18 Q Did anyone at USF&G make an inquiry to 19 better understand the source and the extent of the 20 guarantee for the \$1.162 million?</p> <p>21 A Since it was not properly footnoted, I</p>	<p style="text-align: right;">376</p> <p>1 based upon that there is an insurance policy for which 2 funds will be taken out of, then we had full knowledge 3 that it was an actual event not a potential event.</p> <p>4 Q Well, you couldn't have been confident that 5 the guaranteed portion of the claim was an actual 6 event, right?</p> <p>7 A It didn't say it happened.</p> <p>8 Q Wouldn't it be important for you to know 9 whether it was or wasn't an actual event?</p> <p>10 MR. McGLYNN: Objection.</p> <p>11 A I am assuming that if it happened the 12 footnote would have said the owner failed to pay any 13 part of this claim and enumerated who the owner was 14 because it would be important to outside sources to 15 know the reflection it would have on the jobs in 16 process but it didn't say that. It didn't say anything 17 to that whatsoever. It says if this happens then this 18 will happen. We didn't know that it was going to 19 happen.</p> <p>20 Q And you weren't asking, right? You weren't 21 going to ask whether it was going to happen or not?</p>
<p style="text-align: right;">375</p> <p>1 I don't think anybody did.</p> <p>2 Q What is wrong with the footnote there, sir, 3 that you think should have been more inclusive?</p> <p>4 MR. McGLYNN: Don't raise your voice.</p> <p>5 A Okay. To the extent that it did not 6 specifically say that it was paid, number one it 7 says --</p> <p>8 Q It doesn't say paid, does it?</p> <p>9 A I didn't say that. Could I finish?</p> <p>10 Q Sure.</p> <p>11 A If the owner fails to pay, okay, the 12 insurance company will pay the unpaid portion. That's 13 an insurance policy. It did not say that something was 14 not paid. So we weren't concerned to the extent that 15 we had a unrecognized cost. It stated right here it 16 was just filed and it was a guarantee.</p> <p>17 So from the standpoint of us doing further 18 investigation it would have been more prevalent for us 19 to investigate, we would have I'm sure investigated if 20 it was indicated that there were unpaid portions of 21 unapproved change orders for certain jobs and that</p>	<p style="text-align: right;">377</p> <p>1 MR. McGLYNN: Objection. Asked and 2 answered.</p> <p>3 A I answered that. We didn't ask because it 4 didn't happen.</p> <p>5 Q How do you know why the question wasn't 6 posed?</p> <p>7 MR. McGLYNN: Objection.</p> <p>8 A Because we're dealing with assumptions 9 here.</p> <p>10 Q You mean you're dealing with the assumption 11 that the question wasn't posed because Mr. Salazar 12 didn't have enough information, right?</p> <p>13 A Not correct.</p> <p>14 Q Well, you didn't even take note of this 15 particular sentence about the claim guaranteed by PCIC 16 at the time you received the financial statement, did 17 you?</p> <p>18 A I don't know. I may have and what was 19 important to me is the fact that it did not occur.</p> <p>20 Q Why was it important to you that it -- what 21 didn't occur?</p>

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<p style="text-align: right;">378</p> <p>1 A The fact that the owner failed to pay the 2 claim. It does not say that the owner failed to pay 3 the claim. It only states if the owner fails to pay 4 the claim then such-and-such will be paid. This is not 5 a natural event. Well, doesn't it raise your concern 6 that an owner may not pay. It doesn't say that the 7 owner may not pay.</p> <p>8 Q Didn't the reference that if the owner 9 doesn't pay then PCIC will guarantee the claim raise 10 your concern that the owner may not pay?</p> <p>11 A Again for my underwriter and myself now the 12 fact that it states that there was a claim of 1,162,000 13 filed by the company with a contractor owner doesn't 14 give any information as to the extent of this, who it 15 was, et cetera, therefore if an audited financial 16 statement doesn't make reference to a substantial 17 amount like that, then it would not be important to us. 18 What would be important to us is the fact 19 that there was a policy in effect that if it wasn't 20 paid there was a guarantee of payment there. Now, if 21 that was paid, then it was substantial to the financial</p>	<p style="text-align: right;">380</p> <p>1 CCI; is that true?</p> <p>2 A Where does it say common ownership here?</p> <p>3 Q I'm asking you, sir?</p> <p>4 A No, I did not.</p> <p>5 Q You didn't know that?</p> <p>6 A In looking --</p> <p>7 Q Do you want to go back and look at Exhibit 8 4 and talk about that again?</p> <p>9 MR. McGLYNN: Are you going to raise your 10 voices again?</p> <p>11 A Can I finish my answer?</p> <p>12 Q Go ahead, sir.</p> <p>13 A In looking at this, you understand that in 14 all of the analysis it's done one year apart, number 15 one. Number two, it's done by in this particular case 16 the same underwriter, number three we're dealing with a 17 event that may or may not happen in the future that 18 actually did not happen.</p> <p>19 Q Sir, I asked you a question about whether 20 you understood in 1998 there was common ownership 21 between PCIC and CCI?</p>
<p style="text-align: right;">379</p> <p>1 statement or if it wasn't able to be paid there would 2 be a loss of 1,162,000 in December of 1998. I am sure 3 the question would have been asked and answered.</p> <p>4 MR. McGLYNN: Note that it's 3:30. How 5 much more do you have?</p> <p>6 MR. McCARRON: Not five minutes.</p> <p>7 MR. McGLYNN: Well you know --</p> <p>8 MR. McCARRON: Well what?</p> <p>9 MR. McGLYNN: It's 3:30 if you have five 10 minutes I can stay for five minutes but --</p> <p>11 MR. McCARRON: Let me finish this issue and 12 I'll talk to you for a second if I can.</p> <p>13 MR. McGLYNN: Are you talking to yourself?</p> <p>14 MR. McCARRON: I'm sorry no, I was talking 15 to you. I said let me finish this little thing in two 16 minutes and then we'll talk about what we're going to 17 do.</p> <p>18 MR. McGLYNN: All right. Two minutes.</p> <p>19 Q Sir, you knew as of 1998 when you received 20 the financial statement for 1998 which was Phillips 21 Exhibit 5 that PCIC was owned by common ownership with</p>	<p style="text-align: right;">381</p> <p>1 MR. McGLYNN: Objection.</p> <p>2 A No.</p> <p>3 Q You didn't so --</p> <p>4 A From this statement, no.</p> <p>5 Q No, I didn't ask you that, sir. From 1998 6 were you aware there was common ownership between PCIC 7 and CCI?</p> <p>8 A No.</p> <p>9 Q So that you didn't learn anything from the 10 1995 financial statement which is Phillips Exhibit 2 11 footnote seven which said that PCIC and CCI are owned 12 by the same sole shareholder?</p> <p>13 MR. McGLYNN: Objection.</p> <p>14 A Can I answer that?</p> <p>15 MR. McGLYNN: You may answer.</p> <p>16 A Are you saying that I'm to go from 1995 17 through 1998 and automatically assume that since the 18 footnote didn't state the same statement as it did 19 in '95 and there are number of notes, there are a 20 number of companies that we handle that I should have 21 remembered from three or four years ago?</p>

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<p style="text-align: right;">382</p> <p>1 Q Does the phrase which appears under 2 footnote eight for Phillips Exhibit 5 after the 3 reference to Pennsylvania Contractors Insurance Company 4 a corporation under common control has no significance 5 to you?</p> <p>6 MR. McGLYNN: Jeff, this has been asked and 7 answered.</p> <p>8 Q Not for 1998 it hasn't?</p> <p>9 MR. McGLYNN: Ask him one more time and 10 we're going to suspend and do something, but I'm not 11 going to listen to this for the tenth time. Objection.</p> <p>12 A Under common control could mean a number of 13 people are involved with that. So it didn't mean 14 anything to me in that regard.</p> <p>15 Q Sir, it's a related party under the head 16 note -- I'm sorry let me start over.</p> <p>17 The phrase a corporation under common 18 control appears under footnote headed related party 19 transactions, doesn't it?</p> <p>20 A Yes, it does.</p> <p>21 Q And that wouldn't alert you to the</p>	<p style="text-align: right;">384</p> <p>1 Q All right.</p> <p>2 MR. McGLYNN: The levity is not 3 appropriate.</p> <p>4 MR. McCARRON: We're stopping today because 5 Mr. Phillips and Mr. McGlynn, I believe, is that true, 6 have to leave?</p> <p>7 MR. McGLYNN: Well, I have a plane to catch 8 and as I indicated to you earlier we gave you until 9 3:30. You've had the full day of Mr. Phillips earlier 10 this month. You've also had until 3:30 today and we 11 worked up until about 10 minutes we worked through 12 lunch almost nonstop with a few breaks. As far as 13 we're concerned at this particular juncture either we 14 have ended unless we can make some arrangements at some 15 point in time to finish up. How much more time do you 16 feel you have right now?</p> <p>17 MR. McCARRON: I believe we could probably 18 get done within two hours hopefully less.</p> <p>19 MR. McGLYNN: Now you said three hours ago 20 you had three hours left.</p> <p>21 MR. McCARRON: It wasn't quite three hours.</p>
<p style="text-align: right;">383</p> <p>1 possibility that PCIC and CCI are commonly owned or 2 controlled?</p> <p>3 MR. McGLYNN: Objection.</p> <p>4 A Not by who.</p> <p>5 Q I didn't ask you that question. Well did 6 you have an understanding about the ownership and 7 control of CCI?</p> <p>8 A The ownership and control of CCI?</p> <p>9 Q Yes.</p> <p>10 A Yes.</p> <p>11 Q Who owned and controlled CCI?</p> <p>12 A John Ortenzio.</p> <p>13 Q Well then wouldn't it -- wouldn't you be 14 prompted to realize that PCIC was owned and controlled 15 by the same person as CCI when you read a company -- a 16 corporation under a common control which is a phrase 17 appearing after PCIC under a footnote identified as 18 related party transactions?</p> <p>19 A No.</p> <p>20 Q It wouldn't?</p> <p>21 A No.</p>	<p style="text-align: right;">385</p> <p>1 MR. McGLYNN: About 12:15 now it's 3:30. 2 Now you have three hours.</p> <p>3 MR. McCARRON: The questioning of 4 Mr. Phillips is a slow process for many reasons.</p> <p>5 MR. McGLYNN: Quit the ad hominem attacks, 6 if you're not insinuating that he's taking time or 7 being slow on purpose.</p> <p>8 MR. McCARRON: Not at all.</p> <p>9 MR. McGLYNN: You hesitated between 10 sentences, half sentences.</p> <p>11 MR. McCARRON: Sir, my comment was not 12 intended to be critical of the witness. It was meant 13 to be that it takes time in questioning and simply 14 because there's a lot of time associated with the 15 questioning.</p> <p>16 MR. McGLYNN: You've gone over and over --</p> <p>17 MR. McCARRON: Are you going to let me 18 finish?</p> <p>19 MR. McGLYNN: No, as far as I'm concerned, 20 the deposition has ended. If you want to get back to 21 me some time later on and give me a good faith estimate</p>

Tony Phillips (Vol. II) - 5/29/02

<p style="text-align: right;">386</p> <p>1 of how much for time, if any, you need of Mr. Phillips 2 I'll consider it. You've gone way over the allotted 3 time. We have given you until 3:30 today working 4 through lunch and that's it. I've got a plane to 5 catch.</p> <p>6 MR. McCARRON: All I wanted to do is state 7 my position is, one, the questioning did not go quickly 8 in part because the witness takes time answering the 9 questions. I am not finished my questions as I've 10 clearly indicated to you. We're stopping to 11 accommodate your schedule and Mr. Phillips who has 12 other obligations or schedules to meet and so with that 13 I am agreed to accommodate you. I'm asking that you 14 provide or produce Mr. Phillips on another occasion 15 which hopefully we can schedule in order to complete 16 the deposition.</p> <p>17 MR. McGLYNN: I want from you prior to that 18 a good faith estimate of the amount of time that we 19 need for Mr. Phillips and since we're going to be down 20 in Harrisburg on some other depositions, maybe we can 21 fit Mr. Phillips in at a time that is mutually</p>	<p style="text-align: right;">388</p> <p>1 CERTIFICATE OF DEPONENT</p> <p>2</p> <p>3 I hereby certify that I have read and 4 examined the foregoing transcript, and the same is a 5 true and accurate record of the testimony given by me.</p> <p>6</p> <p>7 Any additions or corrections that I feel 8 are necessary, I will attach on a separate sheet of 9 paper to the original transcript.</p> <p>10</p> <p>11</p> <p>12</p> <p style="text-align: right;">_____ Tony Phillips</p> <p>13</p> <p>14</p> <p>15</p> <p>16</p> <p>17</p> <p>18</p> <p>19</p> <p>20</p> <p>21</p>
<p style="text-align: right;">387</p> <p>1 convenient. But I'm not going to sit here and say I'm 2 going to agree to two more hours, four more hours, five 3 more hours, one more hour unless and until you go back, 4 go over your notes and find out what it is that you 5 need out of Mr. Phillips at this point in time which we 6 can agree to fit him in at a mutually convenient time. 7 That's all I have to say.</p> <p>8 MR. McCARRON: Are we done?</p> <p>9 MR. McGLYNN: You're not going to have the 10 last word. I'm leaving now. As far as I'm concerned 11 the deposition is ended or suspended.</p> <p>12 MR. McCARRON: I asked you are you done? 13 That's all I asked you. I am not like you, I don't 14 have to have the last word.</p> <p>15 MR. McGLYNN: You can close the record. 16 (Deposition was adjourned at 3:35 p.m.)</p> <p>17</p> <p>18</p> <p>19</p> <p>20</p> <p>21</p>	<p style="text-align: right;">389</p> <p>1 State of Maryland</p> <p>2 County of Baltimore, to wit:</p> <p>3 I, RONDA J. THOMAS, a Notary Public of the 4 State of Maryland, Baltimore County, do hereby certify 5 that the within-named witness personally appeared 6 before me at the time and place herein set out, and 7 after having been duly sworn by me, according to law, 8 was examined by counsel.</p> <p>9 I further certify that the examination was 10 recorded stenographically by me and this transcript is 11 a true record of the proceedings.</p> <p>12 I further certify that I am not of counsel 13 to any of the parties, nor in any way interested in the 14 outcome of this action.</p> <p>15 As witness my hand and notarial seal this 16 18th day of June, 2002.</p> <p>17</p> <p>18 _____ RONDA J. THOMAS, RPR</p> <p>19 Notary Public</p> <p>20 My Commission Expires: 21 October 1, 2005</p>

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Anthony Phillips
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1 Q Did you share Phillips 7 with Jim Daily?
 2 MR. McGLYNN: Objection. I don't
 3 understand what you mean by share. Did you give him a
 4 copy?
 5 MR. McCARRON: Yes.
 6 MR. McGLYNN: Ask it that way.
 7 BY MR. McCARRON:
 8 Q Did you share it would be the same.
 9 Either give him a copy, hand it to him, the original
 10 you received or otherwise?
 11 A Could be. I am not sure.
 12 Q How would we determine whether you shared
 13 Phillips Exhibit 7 with Jim Daily?
 14 A If you got a copy of this information
 15 from Jim Daily.
 16 Q Did you discuss the information, which is
 17 included in Phillips Exhibit 7 with Mr. Daily?
 18 A I don't remember.
 19 Q Did you have an understanding about the
 20 phrase or the sentence in the third paragraph on the
 21 first page of Phillips Exhibit 7, "CCI can actually use
 22 this as a buffer to offset losses or profit fades in
 23 certain jobs during any given year", referring to PCIC?
 24 A I didn't think of it at the time.
 25 Q Did it occur to you that CCI Construction

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1 MR. McGLYNN: Objection.
 2 THE WITNESS: What do you mean by review?
 3 BY MR. McCARRON:
 4 Q Receive and review the information which
 5 is included. Actually review the financial statements.
 6 A I can say I read the financial
 7 statements.
 8 Q Did you read all of the financial
 9 statements for CCI Construction as they were received
 10 in the ordinary course of business in connection with
 11 the underwriting?
 12 A Yes.
 13 Q The last time, sir, you told us that you
 14 didn't look at the financial statement for 1998. Have
 15 you changed your answer?
 16 A Did I specifically say I did not look at
 17 the financial statement at all or I did not analyze the
 18 financial statement?
 19 Q You did not read the financial statement
 20 for 1998.
 21 A I would look at every financial statement
 22 that came in. Read every financial statement to me
 23 would mean every part of the financial statement. It
 24 possibly could be 1998 I did a peripheral read and
 25 asked my underwriter to do a more thorough read and

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1 was suggesting it could use money from PCIC to improve
 2 its financial condition and offset losses or profit
 3 fades?
 4 MR. McGLYNN: Objection.
 5 THE WITNESS: I didn't think of it at the
 6 time.
 7 BY MR. McCARRON:
 8 Q Does that sentence now suggest to you
 9 that CCI Construction was indicating it could use PCIC
 10 money to improve its financial condition by offsetting
 11 losses and profit fades?
 12 MR. McGLYNN: Objection.
 13 THE WITNESS: That they were using what
 14 kind of funds did you say?
 15 BY MR. McCARRON:
 16 Q PCIC funds.
 17 MR. McGLYNN: Objection.
 18 THE WITNESS: Possibly.
 19 BY MR. McCARRON:
 20 Q Does that sentence have any other
 21 significance to you?
 22 A No.
 23 Q Did you personally review all of the
 24 financial statements in the ordinary course of business
 25 for CCI Construction?

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1 then a more thorough analysis. That's the only reason
 2 I could say I would give an answer that I didn't read
 3 the 1998 financial statement.
 4 Q Are you able to tell us that you reviewed
 5 in detail the financial statements for every year for
 6 CCI Construction?
 7 MR. McGLYNN: Objection. That's not what
 8 he said.
 9 THE WITNESS: No.
 10 BY MR. McCARRON:
 11 Q Did you evaluate the financial statements
 12 for CCI Construction for every year?
 13 MR. McGLYNN: Objection.
 14 THE WITNESS: Again, what do you mean by
 15 evaluate?
 16 BY MR. McCARRON:
 17 Q Did you personally review and evaluate
 18 the financial statement for CCI Construction as they
 19 were received in the ordinary course of business in
 20 underwriting for CCI Construction?
 21 MR. McGLYNN: Objection.
 22 THE WITNESS: Not fully.
 23 BY MR. McCARRON:
 24 Q Isn't it the case that the bear flags for
 25 CCI Construction were never considered green?

U.S. Fidelity v Bruce Br

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Anthony Phillips
6/20/0

1 MR. McGLYNN: Objection.
 2 THE WITNESS: I couldn't say without
 3 seeing all of the financial statements and having an
 4 evaluation done in reference to what you refer to as
 5 bear flags.
 6 BY MR. McCARRON:
 7 Q Were there any financial statements which
 8 you reviewed and analyzed for any year in connection
 9 with CCI Construction for any underwriting process?
 10 A I don't think so.
 11 Q Did the financial statements for CCI
 12 Construction reflect any material change in financial
 13 condition throughout the years there was a bonding
 14 relationship between CCI Construction and USF & G?
 15 A I don't remember.
 16 MR. McGLYNN: Objection. I don't
 17 understand the question.
 18 BY MR. McCARRON:
 19 Q Are you able to tell us whether the
 20 financial condition of CCI Construction is reflected by
 21 the financial statements for each of the years there
 22 was a bonding relationship between USF & G and CCI
 23 Construction reflected any material change in financial
 24 condition?
 25 MR. McGLYNN: Objection.

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Page 44

1 A Possibly.
 2 Q You don't know if there were?
 3 A I don't remember.
 4 Q Did you review the annual review reports
 5 which were prepared for the CCI account?
 6 A Probably.
 7 Q Did you analyze the information included
 8 in the CCI annual review reports?
 9 A I don't remember.
 10 Q I am showing you what has been marked
 11 Salazar Exhibit 7, Salazar 8, Salazar Exhibit 9,
 12 Salazar Exhibit 10, Salazar Exhibit 11. Are those all
 13 annual review reports for the CCI account?
 14 A Yes.
 15 Q Are you able to confirm that there were
 16 annual review reports for the CCI Construction account
 17 prepared by USF & G on an annual basis?
 18 A Yes.
 19 Q Does the information included in the
 20 annual review reports reflect any material change of
 21 financial condition from year to year for CCI
 22 Construction?
 23 A I don't remember.
 24 Q Are you able to review the annual review
 25 reports and tell us whether there was a material change

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Page 44

1 THE WITNESS: If I had the proper amount
 2 of time to review financial information from report to
 3 report, I probably would be able to tell you.
 4 BY MR. McCARRON:
 5 Q Did you review the annual review reports
 6 for the CCI Construction account?
 7 A I don't know what you mean by that.
 8 Q Did you read the annual review reports
 9 for the CCI account?
 10 MR. McGLYNN: Objection. I think he is
 11 having trouble with what you mean by annual review
 12 reports.
 13 BY MR. McCARRON:
 14 Q Were there annual review reports prepared
 15 by Mr. Salazar in connection with CCI Construction?
 16 A Probably.
 17 Q Do you know whether Mr. Salazar prepared
 18 annual reports for the CCI account?
 19 A Possibly.
 20 Q Showing you what is identified as Salazar
 21 Exhibit 7, is that an annual review report for the CCI
 22 Construction account for the year 1993?
 23 A Yes.
 24 Q Were there other annual review reports
 25 prepared for the CCI account?

1 in financial condition from year to year for CCI
 2 Construction?
 3 MR. McGLYNN: Objection.
 4 THE WITNESS: It depends what you mean by
 5 material change.
 6 BY MR. McCARRON:
 7 Q Are you able to tell us from a review of
 8 the annual review reports prepared for the CCI
 9 Construction account whether there was a material
 10 change to the financial condition of CCI Construction
 11 from year to year from an underwriting perspective?
 12 MR. McGLYNN: Objection.
 13 THE WITNESS: No.
 14 BY MR. McCARRON:
 15 Q Why can't you tell us if there was a
 16 material change in the financial condition of CCI
 17 Construction from year to year which was material to
 18 the underwriting process?
 19 MR. McGLYNN: Objection.
 20 THE WITNESS: My definition of material
 21 change and other people's definition of material change
 22 may be different.
 23 BY MR. McCARRON:
 24 Q Well, whose definition of material change
 25 from an underwriting perspective would be important to

JAMES DAILEY

IN THE UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF PENNSYLVANIA
(Harrisburg Division)

UNITED STATES FIDELITY : CIVIL ACTION
and GUARANTY COMPANY :

-vs- : JUDGE KANE

BRUCE BROWN and BROWN :

SCHULTZ SHERIDAN & :

FRITZ : NO. 1:01-CV-00913

Oral deposition of JAMES
DAILY, taken at the Law Offices of SWARTZ,
CAMPBELL & DETWEILER, 1601 Market Street,
34th Floor, Philadelphia, Pennsylvania
19103, on Thursday, April 18, 2002,
commencing at or about 10:08 a.m., before
Kristy Kupiec, a Certified Court Reporter
and Commissioner of Deeds.

REPORTING SERVICE ASSOCIATES (RSA)

A Veritext Company

1845 Walnut Street - 15th Floor
Philadelphia, Pennsylvania 19103

(215) 241-1000

JAMES DAILEY

	190		192
1 Q.	Were you involved in taking over	1 statements prepared by Brown Schultz?	
2 the jobs for which the bonds had been		2 A. No.	
3 issued and handled by CCI Construction?		3 Q. Have you ever been asked to	
4 A. No.		4 consider whether the deficiencies in the	
5 Q. Did you blame anybody for the		5 financial statements prepared by	
6 problem?		6 Brown Schultz as alleged by USF&G were	
7 A. You know, this sort of thing		7 material in any respect to the underwriting	
8 happens. I mean, this is not the first		8 process?	
9 loss that I had been involved with. Do you		9 A. No.	
10 blame people, well, generally, no. I mean,		10 Q. Do you plan to make that	
11 we all did our best, we just missed the		11 determination?	
12 mark or something.		12 A. I have no information.	
13 Q. Do you think that the problem		13 Q. You have no information about	
14 which developed with CCI Construction was		14 that?	
15 predictable?		15 A. Right.	
16 A. No.		16 Q. Is that right?	
17 Q. So do you also agree that you		17 A. Yes.	
18 could not have predicted the problems with		18 Q. How would you determine whether	
19 CCI Construction?		19 the deficiencies in the financial	
20 A. If we would have been able to, we		20 statements of CCI Construction prepared by	
21 would have.		21 Brown Schultz as alleged by USF&G would	
22 Q. Did you criticize anyone who		22 have been material in the underwriting	
23 worked for USF&G?		23 process for the bond program for the USF&G	
24 A. No.		24 customer?	
	191		193
1 Q.	Did you criticize anyone else for	1 A. It's not something I would be able	
2 the problem which developed with CCI		2 to do. I would have to rely on the	
3 Construction?		3 analysis by another CPA.	
4 A. No.		4 Q. If you had the benefit of	
5 MR. McGLYNN: You mean other		5 financial statements which were in	
6 than filing suit against your		6 conformity with the corrections which USF&G	
7 client?		7 contends should have been in the financial	
8 BY MR. McCARRON:		8 statements, in other words, a corrected	
9 Q. Well, did you ever form an opinion		9 form of financial statements in the opinion	
10 that Brown Schultz had formed for the work		10 of USF&G, would you be able to make a	
11 it did for the preparational financial		11 determination about whether underwriting	
12 statements?		12 decisions would have been affected if that	
13 A. I didn't personally, no.		13 information had been provided during the	
14 Q. Did Schultz do anything wrong in		14 underwriting process?	
15 connection with the financial statements?		15 A. I think so.	
16 A. No.		16 Q. What would control your decision	
17 Q. Have you reviewed your Answers to		17 with respect to whether you could determine	
18 Interrogatories, otherwise known as written		18 the impact of --	
19 questions, prepared by USF&G in connection		19 A. I would have to see --	
20 with this lawsuit against Brown Schultz?		20 Q. -- different financial information	
21 A. I don't remember it.		21 on --	
22 Q. Let me ask you this; have you ever		22 A. I would have to see it first.	
23 read any written forms about the criticisms		23 Q. Were you criticized by anyone in	
24 for which USF&G has over the financial		24 connection with the problem which developed	

JAMES DAILEY

<p>1 from CCI Construction?</p> <p>2 A. No.</p> <p>3 Q. Did you have any adverse</p> <p>4 employment experience because of the</p> <p>5 problem which developed with CCI</p> <p>6 Construction?</p> <p>7 A. No.</p> <p>8 Q. What information would you need to</p> <p>9 know in order to determine whether the</p> <p>10 alleged deficiencies with the financial</p> <p>11 statements were material to the</p> <p>12 underwriting material in connection with</p> <p>13 CCI Construction?</p> <p>14 A. If the financial statements were</p> <p>15 restated, I would have to see the</p> <p>16 restatement and I would have to know</p> <p>17 something, I guess, about who did the</p> <p>18 restatement.</p> <p>19 MR. McCARRON: Off the</p> <p>20 record.</p> <p>21 ---</p> <p>22 (Whereupon, at this time a</p> <p>23 discussion took place off the</p> <p>24 stenographic record.)</p>	<p>194</p> <p>1 the hot buttons that we use.</p> <p>2 Q. Do you believe the manner in which</p> <p>3 the accountants treated indirect costs was</p> <p>4 a material item that affected the</p> <p>5 information on the financial statements?</p> <p>6 A. Well, I guess it could be, but I</p> <p>7 don't really know.</p> <p>8 Q. Did you ever complain about the</p> <p>9 manner in which indirect costs were treated</p> <p>10 in the financial statements?</p> <p>11 A. No.</p> <p>12 Q. Did you have any complaint about</p> <p>13 the manner in which the indirect costs were</p> <p>14 treated on the financial statements</p> <p>15 prepared by Brown Schultz?</p> <p>16 A. No.</p> <p>17 Q. Did you ever take notice that the</p> <p>18 manner in which the indirect costs on the</p> <p>19 financial statements was incorrect?</p> <p>20 A. I didn't notice any anomalies.</p> <p>21 Q. Let me ask you this real quick;</p> <p>22 was there a rating system for bond</p> <p>23 customers?</p> <p>24 A. I wish there were. I am not sure</p>
<p>1 ---</p> <p>2 BY MR. McCARRON:</p> <p>3 Q. Do you agree with the request that</p> <p>4 the alleged deficiencies and the financial</p> <p>5 statements would have to be material and</p> <p>6 material change the information in the</p> <p>7 financial statements in order to affect the</p> <p>8 underwriting decisions?</p> <p>9 MR. McGLYNN: Objection.</p> <p>10 THE WITNESS: Yes.</p> <p>11 BY MR. McCARRON:</p> <p>12 Q. Did you take notice in the manner</p> <p>13 in which indirect costs were treated in the</p> <p>14 financial statements prepared by</p> <p>15 Brown Schultz?</p> <p>16 A. No.</p> <p>17 Q. Did it matter to you how indirect</p> <p>18 costs were treated by the accounts in</p> <p>19 connection with the purpose of financial</p> <p>20 statements prepared by Brown Schultz?</p> <p>21 A. Well, that's part of the profit</p> <p>22 and loss generally, I mean what we see any</p> <p>23 way. If there seemed to be an anomaly, we</p> <p>24 would ask a question. But it is not one of</p>	<p>195</p> <p>1 what kind of rating system.</p> <p>2 Q. Was the amount of premium</p> <p>3 determined by risk factors?</p> <p>4 A. No.</p> <p>5 Q. No?</p> <p>6 A. No.</p> <p>7 Q. It was the same price no matter</p> <p>8 who the customer?</p> <p>9 A. Well, we had several rate</p> <p>10 programs. I believe this came in as a</p> <p>11 merit rate customer, and that was because</p> <p>12 so that was the rate USF&G had at the time.</p> <p>13 And this was a file rate. It was filed in</p> <p>14 all of the states. So if they met the</p> <p>15 criteria of the file rate, we gave it to</p> <p>16 them. We had fewer rates for customers who</p> <p>17 didn't meet the criteria.</p> <p>18 Q. What did it require to maintain</p> <p>19 the merit rate?</p> <p>20 A. There are five criteria, and I am</p> <p>21 not sure if I can quite remember them; CPA</p> <p>22 audits, interim work in progress and maybe</p> <p>23 financial statements, net worth exceeding a</p> <p>24 half million dollars. That's three that --</p>

JAMES DAILY

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1 IN THE UNITED STATES DISTRICT COURT
2 FOR THE MIDDLE DISTRICT OF PENNSYLVANIA
3

4 UNITED STATES FIDELITY) DEPOSITION UPON
5 AND GUARANTY COMPANY
6 Plaintiff) ORAL EXAMINATION
7 vs.) OF
8 BRUCE BROWN AND) JAMES DAILY
9 BROWN SCHULTZ SHERIDAN
10 & FRITZ)
11 Defendants)
12

13 -----
14 TRANSCRIPT OF CONTINUED
15 DEPOSITION, taken by and before MARGIE A. ROMEO,
16 Professional Reporter and Notary Public, at the
17 Law Offices of Swartz, Campbell & Detweiler, 1601
18 Market Street, 34th Floor, Philadelphia, PA on
19 Thursday, June 27, 2002 commencing at 10:20 a.m.
20 -----
21
22

23 REPORTING SERVICE ASSOCIATES (RSA)
24 A Veritext Company
25 1845 Walnut Street - 15th Floor
26 Philadelphia, PA 19103
27 (215) 241-1000

JAMES DAILY

<p style="text-align: right;">275</p> <p>1 Q. In what way would correct information 2 have effected the decisions by USF & G to bond or 3 issue bonds for CCI Construction?</p> <p>4 A. Well, we probably wouldn't have given 5 them as much credit as they were getting.</p> <p>6 Q. And how did you make that determination?</p> <p>7 A. We didn't make that determination.</p> <p>8 Q. How did you determine that you, that USF 9 & G may not have given CCI Construction as much 10 bond credit as was given to CCI Construction if 11 the financial statements had correctly reflected 12 the financial information relative to CCI 13 Construction?</p> <p>14 A. Well, the amount of -- the amount of 15 credit you give is directly related to the 16 financial condition of the customer.</p> <p>17 Q. Is that the end of your answer?</p> <p>18 A. Yes.</p> <p>19 Q. Did you determine or did anyone on behalf 20 of USF & G determine the extent to which the 21 credit for bonding extended by USF & G to CCI 22 Construction might have changed if the financial 23 statements had correctly reflected financial 24 condition of CCI Construction?</p>	<p style="text-align: right;">277</p> <p>1 of exactly what would have changed. I know it 2 would have changed. 3 4 BY MR. McCARRON: 5 Q. When you say you would have to see 6 restated financial information, you mean you 7 would have to see corrected or correct financial 8 statements which accurately reflected the 9 financial condition of CCI Construction during 10 the period involved?</p> <p>11 A. Yes.</p> <p>12 Q. Would you need to see information or 13 consider information in addition to the restated 14 financial statements in order to evaluate whether 15 and to what extent underwriting decisions would 16 have been effected by correctly presented 17 financial statements in the underwriting for the 18 CCI bond account?</p> <p>19 A. Well, we would first have to see the 20 restated financial statements, then if we needed 21 additional information for clarification, we 22 might have asked for something else, but I can't 23 identify what it might have been because we don't 24 have that information.</p>
<p style="text-align: right;">276</p> <p>1 A. No.</p> <p>2 Q. Are you able to tell us the extent to 3 which the bonding credit might have changed by 4 USF & G as extended to CCI Construction, if the 5 financial statements had correctly stated or 6 reflected the financial condition of CCI 7 Construction?</p> <p>8 A. No.</p> <p>9 Q. Why can't you tell us?</p> <p>10 A. I would have to see the restated 11 financial statements first.</p> <p>12 Q. If I could just ask a full question.</p> <p>13 A. I thought you were through.</p> <p>14 Q. I understand. I'm not blaming you.</p> <p>15 Why can't you determine the 16 extent to which the credit for bonding extended 17 by USF & G might have changed for the CCI account 18 if the financial statements had correctly 19 reflected the financial condition of CCI 20 Construction.</p> <p>21 MR. McGLYNN: Objection.</p> <p>22 THE WITNESS: I would have to see 23 the restated information first, but even then I 24 don't think I could give you a definitive answer</p>	<p style="text-align: right;">278</p> <p>1 Q. In addition to the restated financial 2 statements, would your evaluation about the, 3 about whether the restated financial statements 4 would have had an impact on underwriting for the 5 CCI bond credited --</p> <p>6 MR. McGLYNN: Objection.</p> <p>7 THE WITNESS: I'm lost.</p> <p>8 MR. McCARRON: I am too. I'm 9 sorry. 10 11 BY MR. McCARRON: 12 Q. Would you need to consider information in 13 addition to the restated financial statements in 14 order to determine whether and to what extent the 15 bond credit by USF & G might have been different 16 for CCI Construction?</p> <p>17 MR. McGLYNN: Objection.</p> <p>18 THE WITNESS: I don't know. 19 20 BY MR. McCARRON: 21 Q. What I'm trying to understand, sir, is 22 would you have to review other information which 23 was already in the possession, perhaps of USF & G 24 and which had been taken into account during the</p>

JAMES DAILY

<p style="text-align: right;">415</p> <p>1 as strong -- the financial condition of December 2 31, '98 was going to be as strong also as the 3 prior year. 4 --- 5 BY MR. McCARRON: 6 Q. Why did you believe on January 5, 1998 7 the financial condition of CCI Construction would 8 be as good as the prior year? 9 A. They told us that. 10 Q. CCI Construction told you that? 11 A. Yes. 12 Q. Did you have any other information to 13 confirm the financial condition of CCI 14 Construction would be as good as the prior year 15 as of January 5th, 1999? 16 A. I don't think so. 17 Q. So you relied on information received 18 from CCI Construction concerning its financial 19 condition when USF & G underwrote, committed to 20 bond CCI Construction during January, 1999; is 21 that right? 22 MR. McGLYNN: Objection. 23 THE WITNESS: I've lost you. 24 What's the verb?</p>	<p style="text-align: right;">417</p> <p>1 Q. Okay. Were you aware in, that in 1997 2 there were bonuses paid to the officers of CCI 3 Construction? 4 A. I don't remember. 5 Q. Does the comment made in the second 6 sentence of the second paragraph by Mr. Dominiani 7 which says they, referring to USF & G asked me to 8 send their congratulations to you and your 9 management staff; is that an accurate reflection 10 of USF & G's position? 11 A. Well, I think that -- I think that was 12 probably from Tony Phillips. 13 Q. So that does not, Mr. Phillips' statement 14 to Mr. Dominiani was not reflective of the 15 enthusiasm of USF & G? 16 MR. McGLYNN: Objection. 17 THE WITNESS: He doesn't say who 18 he met with. He said I had the opportunity to 19 meet with USF & G. It could have been Tony 20 Phillips. It could have been Dave Hussey. It 21 was not me. 22 --- 23 BY MR. McCARRON: 24 Q. Well, I'm just asking. Is that comment</p>
<p style="text-align: right;">416</p> <p>1 --- 2 BY MR. McCARRON: 3 Q. USF & G relied on financial 4 representations or representations concerning 5 financial condition for the coming year based on 6 information -- USF & G relied on representations 7 from CCI Construction about its financial 8 condition when it decided to commit to bonding 9 during January, 1999? 10 MR. McGLYNN: Objection. 11 THE WITNESS: Yes. 12 MR. McCARRON: This has been 13 marked Phillips-6. 14 --- 15 BY MR. McCARRON: 16 Q. Sir, I'm showing you what has been 17 previously marked Phillips-6. It is a letter 18 from Mr. Dominiani to Mr. Ortenzio dated March 5, 19 1998. 20 Are you familiar with this, and 21 it is date stamped USF & G slash BS 0915. 22 Are you familiar with this 23 document, which is Phillips -- 24 A. I don't think so.</p>	<p style="text-align: right;">418</p> <p>1 that USF & G was extending congratulations to CCI 2 in March of 1998 reflective of the sentiment of 3 USF & G? 4 A. Well, as I recall, '97 was a pretty good 5 year. And whoever Dominiani met with, very 6 likely asked him to extend their congratulations 7 for another good year. 8 Q. Okay. You see the next sentence where it 9 says I understand that your operating profit, do 10 you see that, sir? 11 A. Yes. 12 Q. Do you know who he's referring to in that 13 letter? 14 A. Well, this letter is dated March 5, 1998 15 so it wouldn't have been the three percent, five 16 percent discussed in the January, '99 meeting. 17 So, no, I don't understand. I don't know what it 18 refers to. 19 Q. Does this letter, Phillips-6 refresh your 20 recollection about whether there were minimum 21 equity requirements or ratios of work program? 22 What you are looking at, sir? 23 A. Oh, this is Phillips-6. Does this 24 refresh my recollection?</p>

David Hussey - 5/28/02

1

1 IN THE UNITED STATES DISTRICT COURT
2 FOR THE EASTERN DISTRICT OF PENNSYLVANIA

3 UNITED STATES FIDELITY
4 and GUARANTY COMPANY

5 Plaintiff

6 vs.

CIVIL ACTION NO:
NO. 1-01-CV-00813

7 BRUCE BROWN and BROWN,
SCHULTZ, SHERIDAN & FRITZ

8 Defendants

9

10 The deposition of DAVID HUSSEY was held on
11 Tuesday, May 28, 2002, commencing at 10:00 A.M., at the
12 Law Offices of The St. Paul Companies, 5801 Smith
13 Avenue, Baltimore, Maryland 21209, before Ronda J.
14 Thomas, Notary Public.

15 APPEARANCES:

16 PETER B. MCGLYNN, ESQUIRE
17 On behalf of Plaintiff

18 JEFFREY B. MCCARRON, ESQUIRE
19 On behalf of Defendants

20

21 REPORTED BY: Ronda J. Thomas, RPR

David Hussey - 5/28/02.

<p style="text-align: right;">142</p> <p>1 that USF&G would insist the three percent working 2 capital and a five percent net worth would be, if it 3 was below those amounts, would be corrected in advance 4 of bonding?</p> <p>5 A In advance of issuing final bonds, yes.</p> <p>6 Q So is it the situation then that there 7 should not have been any bonds issued by USF&G while 8 CCI had a working capital less than three percent 9 and/or a net worth less than five percent?</p> <p>10 MR. McGLYNN: Objection.</p> <p>11 A Without an understanding of how that would 12 be corrected there shouldn't have been any bonds 13 issued.</p> <p>14 Q What would satisfy the criteria of an 15 explanation for the manner in which CCI would correct 16 the deficiency below three percent working capital and 17 the deficiency below five percent net worth in order to 18 qualify for bonding?</p> <p>19 MR. McGLYNN: Objection.</p> <p>20 A There would have to be an infusion of money 21 that would bring the deficient, the deficiency, whether</p>	<p style="text-align: right;">144</p> <p>1 deficiency was going to be corrected.</p> <p>2 Q But the correction didn't have to occur in 3 advance of the actual issuance of bonds, is that true 4 or commitment to bond?</p> <p>5 MR. McGLYNN: Objection.</p> <p>6 A No, it's not true.</p> <p>7 Q Tell me why I'm wrong?</p> <p>8 A No, no, in most instances you would want 9 the correction to occur because the only leverage you'd 10 have is the bond, giving them the bond. So by holding 11 back the bond usually we'd get concurrence. But if 12 you're dealing with an account that you have developed 13 a trust and a relationship with and have no reason to 14 doubt if they say they're going to correct it but they 15 have to do -- they have to sell a piece of property or 16 they have to liquidate a stock portfolio, you know, 17 they have the means to get the money in but it will 18 take a certain amount of days, 30, 45 days whatever. 19 There are instances when on the promise, on that kind 20 of a situation on that kind of promise the bonds would 21 be issued because it's a give and take.</p>
<p style="text-align: right;">143</p> <p>1 it be in working capital or net worth, to re-establish 2 it.</p> <p>3 Q To reach the minimum levels; is that right?</p> <p>4 A Yes.</p> <p>5 Q Now, did the infusion of money or other 6 means by which to reach net worth have to occur in 7 advance of the issuance of bonds or was it simply 8 sufficient to have an explanation or a means by which 9 to ultimately reach the minimum threshold amounts for 10 working capital and net worth in order to receive 11 bonds?</p> <p>12 A As long as there was an agreement between 13 the parties as to how the deficiencies would be 14 corrected, Jim Daily was in complete control to do 15 whatever.</p> <p>16 Q Just to be clear, the deficiency below 17 three percent working capital and five percent net 18 worth didn't have to be resolved before bonds would be 19 approved or could be approved for CCI; is that true?</p> <p>20 A That's true as long as there was an 21 agreement. As long as somebody understood how the</p>	<p style="text-align: right;">145</p> <p>1 Q So it was acceptable to issue bonds in 2 spite of working capital below three percent and net 3 worth below five percent provided there was an 4 understanding about the means by which CCI would 5 quickly come into conformity with the three percent 6 working capital requirement and the five percent net 7 worth requirement; is that right?</p> <p>8 A Yes, that's correct.</p> <p>9 Q What was your tolerance for a change in the 10 financial condition of CCI before you would withhold 11 approval for bonding?</p> <p>12 MR. McGLYNN: Objection.</p> <p>13 A In accounts of this size and this nature 14 doing the volume that it's doing, that they were doing, 15 and the fact that you have a substantial amount of 16 bonded work underway or exposure you would -- the 17 tolerance would be -- you couldn't cut and run. You 18 couldn't just wake up one day and say I'm not going to 19 give them anymore bonds because you'd be laying 20 yourself exposed. Because for whatever reason that you 21 have come to that conclusion would be the exact reason</p>

David Hussey - 5/28/02

<p style="text-align: right;">146</p> <p>1 no other surety would give them credit. 2 So the tolerance, the tolerance wouldn't -- 3 you would certainly react strongly to losing half their 4 net worth but you wouldn't expect an account of this 5 size and stature to disintegrate overnight considering 6 the track record of the firm. Therefore, there should 7 be in instances of this sort enough time to react to a 8 negative situation and give them a chance to rebound. 9 Q Well, would a loss of 50 percent of net 10 worth be enough to change the financial condition of 11 CCI so that bonding approval would have been withheld? 12 MR. McGLYNN: Objection. 13 A It's speculative. 14 Q Why is it? 15 A Because a loss of 50 percent of the net 16 worth would have shocked -- would have driven -- would 17 have left us shellshocked. The fact of the matter is 18 is when these guys hit the wall I was stunned, I am 19 still stunned today that they disintegrated as quickly 20 as they did. There was no time to react. 21 Q To what degree would you have allowed a</p>	<p style="text-align: right;">148</p> <p>1 greater? 2 MR. McGLYNN: Objection. 3 A In this instance no because by the time we 4 would catch up to the fact that the fluctuation had 5 occurred steps had already been taken to reverse the 6 situation and to bring the net worth back. So that 7 they had proven to us that they could manage their 8 peaks and valleys. 9 Q Well, to what degree did the financial 10 condition as reflected on the financial statements of 11 CCI have to change in order to prompt a decision by 12 USF&G not to continue to approve bonds? 13 MR. McGLYNN: Objection. 14 A Well, the answer to that would have been 15 the fact they called a meeting in October of 1999 and 16 said they were in trouble that they needed assistance 17 and we instituted a call to our claim department to go 18 out and look at the situation. So you have a situation 19 where you have the answer to your question in terms of 20 when they called the meeting to say they were having 21 temporary cash flow problems that John Ortenzio was</p>
<p style="text-align: right;">147</p> <p>1 change in net worth before the change in net worth 2 would have an impact adversely on underwriting? 3 MR. McGLYNN: Objection. 4 Q For CCI? 5 MR. McGLYNN: Objection. 6 A Almost any -- with CCI in terms of the 7 underwriting change in net worth of a half a million 8 dollars would have caused a concern so that we -- yeah, 9 we would have watched a negative situation very closely 10 considering the fact that over the course of the last 11 few years they had managed to reverse unprofitable 12 interim results and they had always been showing signs 13 of managing their problems. So that they had showed 14 signs that they were on top of situations well before 15 we were or could have been. 16 Q Well, the net worth of CCI fluctuated by 17 amounts greater than \$500,000 over the course of the 18 bonding relationship with USF&G, didn't it? 19 A Right. 20 Q Did it cause USF&G alarm and concern every 21 time the net worth fluctuated or reduced by \$500,000 or</p>	<p style="text-align: right;">149</p> <p>1 going to the bank for more money. 2 There was enough concern with that 3 conversation to cause us to turn to our expertise to 4 send in the auditors and the project evaluation, to go 5 through the project evaluation to see -- just to take a 6 forensic look at the firm to see what was wrong. What 7 was the problem. 8 Q So did it have to be a financial change as 9 extreme as what was discovered at the end of 1999 for 10 USF&G to decide not to continue to approve bonds for 11 CCI? 12 MR. McGLYNN: Objection. 13 A The situation blossomed very quickly and it 14 was -- 15 Q You're speaking about the situation at the 16 end of 1999? 17 A Yes. 18 Q But what I'm asking is, along the 19 relationship, along the way with the relationship 20 between USF&G and CCI to what extent did the financial 21 condition as reflected by CCI on the financial</p>

1 UNITED STATES DISTRICT COURT
2 FOR THE MIDDLE DISTRICT
3 OF PENNSYLVANIA
4 HARRISBURG DIVISION

5 * * * * *

6 UNITED STATES FIDELITY *
7 AND GUARANTY COMPANY, *

COPY

8 Plaintiff * Civil Action

9 vs. * No. 1:01-CV00813

10 BRUCE J. BROWN and BROWN *

11 SCHULTZ SHERIDAN & FRITZ, *

12 Defendants *

13 * * * * *

14 DEPOSITION OF

15 BRUCE BROWN

16 JULY 19, 2002

17

18

19

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22 by the certifying agency

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1 Q. Was that your opinion with respect to the
2 1998 audit, that because it was a covered claim, you
3 could look at it as revenue.

4 ATTORNEY CARSON:

5 I object to the form, it
6 mischaracterizes his testimony.

7 A. I'm going to state one more time, I think
8 that we had two pieces here. I think that we looked
9 at the guarantee we felt that, number one, the
10 guarantee indicated that PCIC, for whatever reason,
11 the related party basically, they agreed that should
12 DGS, the Department of General Services, not recognize
13 the claim, that to the extent that the claim went
14 unrecognized that they would submit to the claim.

15 We also. And I refer to the work paper
16 which is your Exhibit 20, the second page of that, we
17 also made the statement that per review of the policy,
18 it says PCIC will be reimbursed for all costs
19 reasonably performed in conjunction with fulfilling
20 its obligations. So I think that further solidified
21 why PCIC would even provide the guarantee, that there
22 was basis for PCIC having a claim against it. They
23 provided guarantee which guaranteed that the amount of
24 the \$1,162,460 was going to be recovered by CCI in
25 some shape or form, and which essentially it did

1 happen in 1999.

2 BY ATTORNEY MCGLYNN:

3 Q. Why the need for the guarantee if it were
4 fully covered under the remedial work insurance
5 policy?

6 A. I didn't request the guarantee, to the best
7 of my recollection, although I can't say that I did
8 have a conversation with Sheri Phillips. I don't
9 recall that, to be honest to you.

10 Q. Was there any question in your mind as to
11 whether or not the Claimant in Exhibit 20 was fully
12 covered by the remedial insurance policy?

13 ATTORNEY CARSON:

14 Object to form.

15 A. They provided us a copy of the guarantee, I
16 think, before we audited the claim. So it was
17 management's decision to go this route. It wasn't a
18 requested by Brown, Schultz, Sheridan and Fritz.

19 BY ATTORNEY MCGLYNN:

20 Q. Did you make any determination as to whether
21 or not the guarantee issued by PCIC fully covered the
22 claim in Exhibit 20?

23 A. The guarantee was for \$1,200,000. The claim
24 was for \$1,162,460. The assets of PCIC exceeded the
25 amount of the guarantee.

1 ATTORNEY MCGLYNN:

2 Are you instructing him not to
3 answer?

4 ATTORNEY CARSON:

5 Yes.

6 ATTORNEY CARSON:

7 If he can relate it to.

8 (Exhibit 36 marked
9 for identification.)

10 BY ATTORNEY MCGLYNN:

11 Q. Was this \$40,179 and \$84,636 paid to CCI?

12 A. I believe from looking at something you gave
13 me previously, that it was paid to CCI.

14 Q. Take a moment and look at what we've marked
15 as --- I think that is Exhibit 36.

16 A. Yes. What's the question?

17 Q. That was the question. Now that you've
18 reviewed it, I'm going to ask you some questions about
19 it. What is this document?

20 A. This looks to be a work paper that
21 reconciles the total claims incurred back to the work
22 papers in the December 31, 1999, engagement. It's
23 simply an analysis of claims by type and it's just a
24 work paper to reconcile to what's on the company's
25 general ledger.

1 Q. It says claims paid up at the top on the
2 remedial \$942,460, do you see that?

3 A. Right.

4 Q. You do see it?

5 A. Yes.

6 Q. Is that \$942,460, is that the amount that
7 was paid on the Mahanoy prison project?

8 A. Yes.

9 Q. And does that relate to the total payments
10 made as reflected in --- can you read the Exhibit
11 Number ---?

12 A. Exhibit 26.

13 Q. And those payments were made on or after
14 June of 1999?

15 A. Under item A tick mark it shows when three
16 payments were made, making up the \$942,460 paid on
17 June 28th, \$72,460 on September 8th and \$70,000 on
18 September 24th.

19 Q. How was this payment booked on PCICS
20 records?

21 A. As claim paid.

22 Q. Claim under the remedial insurance policy?

23 A. Yes.

24 Q. As opposed to the guarantee?

25 A. They only had one classification of

1 expense. So that's what it was booked as.

2 Q. And how is it booked on the CCI side of
3 things?

4 A. I didn't do work for CCI in 1999. So I have
5 no idea.

6 Q. Again, referring to this most recent
7 exhibit, what is that?

8 A. Thirty-six (36).

9 Q. It also indicate that \$220,000 was paid on
10 the claim on the Mahanoy prison claim from the
11 Department of General Services?

12 A. Correct.

13 Q. And down below, the payments to CCI and it
14 has 6/28/99, \$800,000 and then the two payments in
15 September of 1999. Those are the dates when the
16 payments were made to CCI?

17 A. Correct.

18 Q. Thank you. Now, the final payment to CCI
19 for this Mahanoy prison claim was made on the 24th of
20 September, according to this exhibit?

21 A. Yes.

22 (Exhibit 37 marked
23 for identification.)

24 BY ATTORNEY MCGLYNN:

25 Q. Can you identify that letter, which we've

UNITED STATES FIDELITY AND GUARANTY CO. V
BRUCE J. BROWN

WITNESS: BRUCE BROWN

DATE: JULY 19, 2002

EXHIBITS: 1-4A, 18-39

**SPHERION DEPOSITION SERVICES
545 FIFTH AVENUE, SUITE 900
NEW YORK, NEW YORK 10017**

0000 77149

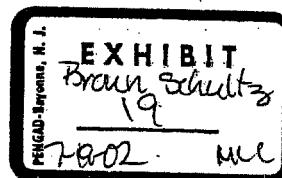
GUARANTY AGREEMENT

This Guaranty Agreement, given on this first day of December, 1998, by PENNSYLVANIA CONTRACTORS INSURANCE COMPANY ("PCIC") to CCI CONSTRUCTION CO., INC. ("CCI") as follows:

PCIC will guarantee the claim that was filed by CCI, in the amount of One Million One Hundred Sixty-Two Thousand Four Hundred Sixty Dollars (\$1,162,460.00), with the Department of General Services, Commonwealth of Pennsylvania, for the project known as Mahanoy State Correctional Institution, Frackville, Pennsylvania. If the Department of General Services, Commonwealth of Pennsylvania, fails to pay all or any part of the subject claim, PCIC will pay the difference owing or the full amount of the claim if no part of the claim is paid.

All rights and liabilities herein given to, or imposed upon, the respective parties hereto shall extend to and bind the several and respective heirs, legal and personal representatives, successors and assigns of said parties. No rights, however, shall inure to the benefit of any assignee of CCI unless the assignment to such assignee has been approved by PCIC.

This writing contains the entire agreement between the parties hereto, and no agent, representative or officer of either party has authority to make or has made any statement, agreement or representation, either oral or written, in connection herewith, modifying, adding or changing the terms and conditions herein set forth. No dealings between the parties or custom shall be permitted to contradict various additions to or



	Remedial	Reinsured	Total
Claims paid	(1) 942,460.00	(a) 72A 3,030.35	945,490.35
Claims payable	0.00 (b)	0.00 (c)	0.00
Claims reserve - beginning	(862,338.00)	0.00	(862,338.00)
Claims reserve - ending	0.00 (b)	0.00 (c)	0.00
Claims incurred	80,122.00	3,030.35	83,152.35
Per general ledger		83,152.35	
Difference		0.00	
(a) Total Mahanoy Prison claims Less: Payment Dept Genl Services	1,162,460.00 (220,000.00)	Per Sheri Phillips & John Olenzio Settlement amt 942,460.00 (1)	
Payment to CCI	06/28/99 800,000.00		
"	09/08/99 72,460.00		
"	09/24/99 70,000.00		
		942,460.00	
Difference		0.00	
(b) Policies all expired through 9/30/99 (last policy written was Outlook Pointe; policy began 9/30/98 for one year term. Policies are written on claim made basis, therefore the insured has until end of policy to submit claims. Per Sheri Phillips 1/20/2000, there were no claims reported.			
(c) The Consumers Reinsurance Company reinsurance contract was terminated effective 5/31/99; therefore no claim liabilities exist at 12/31/99; See termination agreement and recapture calculation at 82			